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SUBJECT: NIGERIA: CENTRAL BANK INCREASES MONETARY POLICY RATE

REF: A. 07 ABUJA 2417

1B. 07 ABUJA 2227

1C. 07 ABUJA 1793

11. SUMMARY: The Central Bank of Nigeria (CBN) has raised its Monetary Policy Rate (MPR) from 9.5% to 10% in April. This is the second increase in four months. A higher MPR increases the cost of borrowing and should encourage savings, but has not. The Nigerian interest deposit savings rate has decreased from 3.77% in July 2007 to 2.86% in February 2008. In March 2008, the average interest savings rate was 2.92% and yet average lending rate was 16.20% leading to an unhealthy gap between savings deposit and lending rates. END OF SUMMARY

12. On April 1, 2008, the Central Bank of Nigeria (CBN) raised the Monetary Policy Rate (MPR) by 50 basis points, from 9.5% to 10 %, citing recent GON fiscal activities. It is the second increase in four months. The MPR is the interest rate at which the CBN lends money to the commercial banks, and according to the CBN, their goal with the MPR is to adjust short-term interest rates to maintain a stable national currency, low inflation, and economic growth.

13. In June 2007 when the MPR was reduced by 200 basis points, commercial banks prime lending rate fell only by 48 basis points from 16.94% to 16.46% and rate on customer deposits fell by 77 basis points from 3.82% to 3.05%. Between July 2007 and March 2008, the MPR rose by 150 basis points, but the commercial banks' savings and time deposit rates declined steadily from 3.77% to 2.86%.

14. COMMENT: Clearly, interest rates by commercial banks in Nigeria do not react proportionately to adjustments in the MPR. So far the increases in the MPR have led only to increasing borrowing costs to contain inflation, but failed to encourage savings. A higher MPR limits lending credit for increasing production capacity, employment generation, and hinders business cost competitiveness. In March 2008, the average interest savings rate was 2.92% and yet average lending rate was 16.20% leading to an unhealthy gap between savings deposit and lending rates. END COMMENT.